

SUBJECT: Security interests in farm products

COMMITTEE: Agriculture and Livestock: committee substitute recommended

VOTE: 8 ayes--Saunders, Robinson, Harrison, Earley, Edge, Kubiak, Patterson, Perry

0 nays

1 absent--Carriker

WITNESSES: For--Jim Schwertner, Schwertner State Bank; Roy Wheeler, Independent Cattlemen's Association; Zay Gilbreath, Texas Cattle Feeders Association; Don Graham, Texas Grain and Feed Association; Steve Purcell, Livestock Insurance Services, Inc.; Adolph Hanslik, cotton merchant; Nancy Patton, cotton merchant

Against--Jim Lederer, Texas Bankers Association; Don Adams, Independent Bankers Association of Texas; Jay Godwin, Texas Bankers Association

BACKGROUND: Under current law, a person who buys an item in the ordinary course of business generally buys it free and clear of any debt owed by the seller, even if the seller has used the item as collateral for a loan. Purchases of farm products are an exception to this general rule. When a farm product that has been pledged as collateral for a loan is sold by a farm operator, the lender does not lose the right to take the product to satisfy the farm operator's debt, even if the buyer had no knowledge of the loan when the farm product was purchased.

A farm product is defined in the law as crops or livestock or supplies used or produced in farming operations or products of crops or livestock in their unmanufactured state (e.g., ginned cotton, milk, eggs).

DIGEST: CSHB 1741 would change the procedure for establishing and retaining a security interest (right to take an item to satisfy a debt) on farm products.

This bill would allow the lender with a security interest in a farm operator's products to enforce that interest against someone who bought the products only

DIGEST: if the lender sends the buyer a notice of the security
(continued) interest by certified mail within 90 days of the day
the products were sold.

This bill would change the place for filing the documents necessary to perfect a security interest in farm products (i.e., establish precedence over other creditors who might want to sell the collateral to satisfy other debts of the farm operator). The place for such filings would change from the office of the county clerk to the office of the Secretary of State. Continuation statements, to keep the security interest effective after its initial five-year term, would also be filed with the Secretary of State.

A separate part of the bill would affect security interests generally, not just those pertaining to farm products. This part of the bill would amend sec. 32.33(f) of the Penal Code, which makes it a crime to sell secured property (property used as collateral for a loan) without the secured party's consent, if the person selling the property intends to "appropriate" the secured party's interest. The seller would be presumed to have intended to appropriate the interest if he or she did not turn over the proceeds to the secured party or account for the proceeds to the secured party within ten days after receiving a lawful demand for the proceeds or account. The crime, hitherto graded according to the amount of the unpaid balance remaining on the secured debt, would now be punished according to the amount of the proceeds received from the sale.

SUPPORTERS Buyers of farm products that have been pledged
SAY: as collateral for loans have no protection against the possibility of having to pay twice for the products. They may have to pay once to the seller of the products, and a second time to the lender to whom the products were pledged as collateral. CSHB 1741 will correct this situation, and give buyers of farm products the same protection that buyers of any other item already have while, maintaining the lenders' interests.

Buyers will not be responsible for paying the debt for which the farm product is the collateral unless they are notified of the debt by the lender within 90 days of the sale. Buyers will no longer suddenly find themselves, years after making a purchase, responsible for a debt that was undertaken by the seller of the

SUPPORTERS
SAY:
(continued)

farm product. This provision will not put an undue burden on the lender, since any responsible lender should know when cattle are likely to be auctioned or a crop is about to be harvested.

Merchants who buy farm products have no simple means of checking for the existence of liens on products they buy. Liens are currently filed in the county clerk's office where the debtor lives, or where the products were located, or wherever the chief executive office of a corporate farm is located. This bill will centralize all filing of liens in the Secretary of State's office, where they will be easily accessible to merchants doing business in any part of the state. Since filing can be done by mail, it will not be any more difficult for lenders than filing in a county clerk's office. These centralized files could eventually be made available by computer to a buyer's home terminal.

As a protection to lenders, the criminal provisions against hindering a creditor will be strengthened. It is sometimes difficult to prove that the seller of a secured property had the intent to deprive the secured party of the proceeds of the sale. This bill establishes a clear deadline by which the seller must notify the lender of the sale or give the lender the proceeds of a sale. If that deadline is not met, a jury must presume that the seller did intend to deprive the secured party of the proceeds.

OPPONENTS
SAY:

This bill offers little improvement over the current law. A buyer could still be found responsible for a debt 90 days after a purchase, if the lender sent the proper notice. Since it is likely that the Secretary of State will not be able to organize and make accessible the large number of filings this bill will generate, there will still be no easy way for a buyer to be sure that a farm product is not pledged as collateral on a loan. Farm products should be treated just like any other good, so that a buyer is free of responsibility for a debt undertaken by the seller.

NOTES:

A bill to change the grading of the crime of hindering a secured creditor (HB 321 by Robinson) passed the House on April 16 and was referred to the Senate Jurisprudence Committee on April 18.